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**STATE WATER RESOURCES CONTROL BOARD  
BOARD MEETING SESSION - DIVISION OF FINANCIAL ASSISTANCE  
JULY 19, 2006**

## ITEM 5

### SUBJECT

CONSIDERATION OF A RESOLUTION TO AUTHORIZE A STATE REVOLVING FUND (SRF) LOAN TO THE CONSERVATION FUND (CF) FOR THE BIG RIVER/SALMON CREEK CONSERVATION FORESTRY ACQUISITION (PROJECT), SRF LOAN NO. C-06-6090-110

### DISCUSSION

The CF is a 501(c)(3) non-profit corporation based in Arlington, Virginia. The CF works with government agencies, corporations, foundations, and willing landowners to protect wildlife habitat, forestlands, recreation areas, open spaces, working landscapes, and historic places. Since its founding in 1985, the CF and its partners have protected more than five million acres. The CF has considerable expertise in forest management, and currently owns or manages productive forestland in New York, North Carolina, Vermont, Virginia, and California.

The CF submitted an application to the State Water Board requesting a \$25 million loan from the SRF program to acquire 11,600 acres of forestland in the Big River watershed (Big River Tract) and 4,345 acres of forestland in the Salmon Creek watershed (Salmon Creek Tract). The CF has reached a preliminary agreement with the owner, Hawthorne Timber Company (HTC) of Mendocino County, to acquire both parcels for \$48.5 million by September 2006. Both properties are currently being used by HTC for industrial timber production.

Acquisition of the two properties will significantly contribute to the CF's goal of protecting and enhancing beneficial water uses along the North Coast by establishing a model forest, fisheries, and watershed project through acquisition and management of fee title or conservation easements. Acquisition of the Big River and Salmon Creek properties will bring the total acreage under the CF's management in California to approximately 50,000 acres. In addition to this acquisition, HTC and the CF have agreed to discuss the eventual sale of a working forest easement on approximately 165,000 additional forestland acres contiguous with the Big River parcel.

The Water Quality Control Plan (Basin Plan) for the North Coast Regional Water Quality Control Board (North Coast Regional Water Board) identifies a number of beneficial uses that have been impaired in North Coast watersheds by sediment related to industrial timber harvesting. The Big River is listed on the 303(d) list as impaired for sediment and temperature, and a Total Maximum Daily Load (TMDL) for sediment has been adopted for the Big River by the North Coast Regional Water Board. Salmon Creek is not currently 303(d) listed for any pollutants, however, acquisition of the Salmon Creek Tract and the implementation of management measures by the CF will prevent the deterioration of Salmon Creek and help prevent 303(d) listing in the future.

By acquiring the land, the CF will help protect and restore water quality, aquatic and terrestrial habitat, and other forest resources. The CF will acquire the two properties with the understanding that they will reduce harvest rates by about 40 percent from those levels allowed under the current Forest Practices Rules, prepare new Timber Harvest Plan (THP), and implement, in cooperation with the North Coast Regional Water Board and other groups in the area, restoration activities and appropriate management practices consistent with the "Plan for California's Nonpoint Source Pollution Control Program" (NPS Plan) to address the TMDL in the Big River watershed and prevent further deterioration of the Salmon Creek watershed. Acquiring the properties will also result in permanently protecting them from subdivision, mining, water diversion, and conversion to non-forest uses such as vineyard development. The SRF loan agreement will include conditions that will ensure that the CF follows through with the agreed upon measures for the two properties, and the State Water Board will be included on the deed as a beneficiary until the loan has been repaid.

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Although the North Coast Regional Water Board has adopted the Big River TMDL for sediment, an implementation strategy or action plan has not been developed for the sediment TMDL. Since there are no specific management measures outlined in the current THP's consistent with the proposed change in harvest levels and management methods, the loan agreement will require that no later than two years after the acquisition of the two properties, the CF will develop a water quality management and restoration plan (WQMRP). This plan will explain the measures the CF will implement to correct and prevent deterioration of the watersheds due to past, current, and proposed timber harvest practice, and how performance and benefits of the Project will be measured. This plan must be submitted for review and approval by the North Coast Regional Water Board staff; a copy must be submitted to the State Water Board also. The measures outlined in the WQMRP will also be implemented in future THP's for the Project.

In the interim, the CF will manage the properties in accordance with management measures similar to those proposed for the Garcia River Forest Project TMDL and the existing THP's. Although the existing THP's permit clear cut harvesting, the CF will reduce harvest levels to a rate consistent with the operations and management (O&M) plan submitted in their application. These measures will substantially reduce the potential for erosion by reducing disturbances associated with clear cuts and streamside harvests. The CF will also work closely with the North Coast Regional Water Board and other agencies to develop and submit future THP's that are consistent with the approved WQMRP.

The Project meets the requirements of the State Water Board's "Strategy for Implementing the SRF for Expanded Use Projects" as follows:

- The Project is consistent with the State Water Board's Antidegradation Policy by
  - (a) permanently protecting the properties from subdivision, residential and commercial development, forestland conversion, and agricultural intensification, and
  - (b) implementing silviculture management measures identified in the NPS Plan relating to forestry.

The Project is consistent with the NPS Plan making it eligible for SRF funding under Section 319 of the federal Clean Water Act. The Project will allow CF to do Watershed Protection and Forestry Management Measures from the NPS Plan.

The SRF loan will be repaid from revenues derived from timber harvests consistent with the implementation of the silviculture management measures identified in the WQMRP and the revised THP's. Staff reviewed an appraisal prepared for the CF by Gene Forsburg, a Registered Professional Forester and licensed real estate appraiser. The analysis shows that harvest volumes can be decreased significantly from present volumes, but still provide a sustainable yield and significant margin of safety for revenue generation. The appraiser estimates that the total market value of the two properties is \$52.25 million and that the Tracts together will generate annual net revenues of approximately \$3,690,954. The Department of General Services will review the Forsburg appraisal as part of the SCC grant approval for the same project. Execution of the loan agreement is contingent on this appraisal, and other supporting documentation, which supports the conclusion that timber harvests can be reduced to improve water quality and still generate sufficient income to repay the SRF loan and implement the WQMRP measures.

The market for redwood forest products appears robust, contributing half of the annual value of timber harvested in California. In addition, the value of timber has increased steadily over the last three decades. Moreover the risk of catastrophic loss of timber as a source of revenue appears to be low. The CF submitted an O&M plan that includes revenue projections for the projected timber harvest over the next 20 years. State Water Board staff analyzed the plan and calculated the estimated revenues from the reduced timber harvest data. Calculations show that the CF can reduce the harvest level about 44 percent below what Mr. Forsburg calculated as the annual harvest revenue. Using the O&M plan data, the lowest net revenue generated in a given year is estimated to be \$1,567,793 with the average net revenue for a 20 year harvest period around \$1,922,282 for the two

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properties combined. For an SRF loan with an interest rate of 2.4 percent, the annual repayment for the \$25 million loan is estimated to be \$1,590,998. This indicates the net annual average revenue is adequate to repay the SRF loan and provide sufficient funds to manage the properties and implement actions in the WQMRP.

In order to mitigate any possible unanticipated risks or fluctuations in timber volume or market price, the CF has also agreed to establish a repayment reserve. Concurrent with execution of the loan, the CF will be required to establish a loan reserve (Loan Reserve) equal to two years payment of principal and interest (Reserve Amount). The Loan Reserve and any investment earnings may be used to supplement project revenues as necessary to meet loan payments as they come due. In the event the Loan Reserve falls below the Reserve Amount, surplus project revenues will be applied to re-establish the Reserve Amount. Surplus project revenues beyond those necessary to re-establish the Reserve Amount may be used to increase the Reserve Amount to a maximum of three years payment of principal and interest, accelerate the implementation of water quality enhancement measures, or make prepayments of loan principal. Surplus Loan Reserve beyond the Reserve Amount may be used to accelerate the implementation of water quality enhancement measures or make prepayments of loan principal. The WQMRP will establish the criteria for deciding how surplus project revenues and surplus Loan Reserve will be used.

The SRF loan will be used in conjunction with the following to acquire the two properties:

- \$6 million grant from the State Coastal Conservancy (SCC) is set for commitment approval on July 29, 2006.
- \$6 million grant from the Wildlife Conservation Board is set for commitment approval on August 17, 2006.
- \$2 million grant from the National Fish and Wildlife Foundation is set for commitment in November 2006, but the CF will pre-fund the contribution.
- \$6 million grant from foundations and individuals is set for commitment in July 2006.
- \$3.5 million from the CF that was already committed in December 2005.

The SCC filed a Notice of Exemption (NOE) with the Governor's Office of Planning and Research on June 29, 2006, for the proposed Project. A Categorical Exemption from California Environmental Quality Act (CEQA) requirements was applied to the SCC's project because the change in land management from industrial timber harvest to sustainable timber harvest will allow for the preservation of fish and wildlife habitat and preserve the land in a more natural condition. Additionally, the land purchase will allow restoration of aquatic and terrestrial habitats, create water quality improvements, and permanently protect the properties from subdivision, residential and commercial development, forestland conversion, and agricultural intensification. [Class 13: Acquisition of Lands for Wildlife Conservation Purposes, CEQA Guidelines Section 15313 and Class 25: Transfers of Ownership of Interest in Land to Preserve Existing Natural Conditions and Historical Resources, CEQA Guidelines Section 15325]. The CF reviewed the CEQA requirements for this project and determined that it qualifies for a Categorical Exemption under CEQA Guidelines Section 15325. State Water Board staff have reviewed the Project and considered the NOE and determined that the project qualifies for a Categorical Exemption under CEQA Guidelines Sections 15313 and 15325 and will not result in any significant adverse water quality impacts.

## POLICY ISSUE

1. Should the State Water Board approve a Resolution to authorize a SRF Loan for \$25 million to the CF for the Big River/Salmon Creek Conservation Forestry Acquisition Project?
2. Should the State Water Board condition the loan such that the repayment starts one year after the first disbursement?

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## FISCAL IMPACT

(as of 6/6/06)

	SFY 2005-06	SFY 2006-07	SFY 2007-08	SFY 2008-09	SFY 2009-10
Beginning Balance:	\$394,995,892	\$376,725,164	\$121,358,696	\$75,408,404	\$156,029,341
Estimated Repayments	\$173,837,506	\$176,498,725	\$186,498,725	\$196,498,725	\$206,498,725
Debt Service on Revenue Bonds	(\$33,474,879)	(\$33,439,354)	(\$33,357,579)	(\$31,893,104)	(\$31,758,441)
Estimated Capitalization Grants	\$79,435,719	\$44,528,520	\$0	\$0	\$0
State G.O. Bond proceeds (less state admin. match)	(\$606,678)	\$0	\$0	\$0	\$0
Local Match Credits	\$12,252,573	\$26,276,923	\$7,075,635	\$4,610,358	\$4,166,750
Est. SMIF Interest:	\$2,000,000	\$2,000,000	\$2,000,000	\$2,000,000	\$2,000,000
<u>Estimated Disbursements</u>	(\$251,714,969)	(\$365,930,039)	(\$149,110,889)	(\$66,083,477)	(\$50,000,000)
<b>Subtotal</b>	<b>\$376,725,164</b>	<b>\$226,659,939</b>	<b>\$134,464,587</b>	<b>\$180,540,906</b>	<b>\$286,936,374</b>
Rosamond Community Services District, Proj. No. 4148-110		(\$7,500,000)	(\$2,500,000)		
LACSD, Proj. Nos. 4701-110 through 4701-520		(\$9,479,000)	(\$27,097,597)	(\$7,711,565)	(\$204,000)
Sonoma Valley CSD, Proj. No. 4823-110		(\$3,680,000)	(\$3,000,000)		
St. Helena, City of, Proj. No. 6093-110		(\$8,000,000)	(\$3,000,000)	(\$1,000,000)	
Nevada Co., Proj. No. 4969-110		(\$9,129,452)	(\$2,993,408)		
Nevada Co., Proj. No. 4968-110		(\$18,512,791)	(\$465,178)		
Conservation Fund, Proj. No. 6090-110		(\$25,000,000)			
Reserve for Small Community Wastewater Grant Projects		(\$24,000,000)	(\$20,000,000)	(\$15,800,000)	
<b>Balance</b>	<b>\$376,725,164</b>	<b>\$121,358,696</b>	<b>\$75,408,404</b>	<b>\$156,029,341</b>	<b>\$286,732,374</b>

## REGIONAL BOARD IMPACT

Yes, North Coast Regional Water Board.

On April 19, 2005, the North Coast Regional Water Board discussed and approved the addition of the project to the SRF priority list for Region 1. The North Coast Regional Water Board has reviewed the project, and their staff have indicated they will work with the CF to implement measures that will address the Big River sediment TMDL and protection of the Salmon Creek watershed.

## STAFF RECOMMENDATION

1. That the State Water Board approve a Resolution to authorize a SRF Loan in the amount of \$25,000,000 to the CF for the Project
2. That the State Water Board add a condition to the loan agreement that repayment of the loan will start one year after the first disbursement.

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## STATE WATER RESOURCES CONTROL BOARD RESOLUTION No. 2006 –

### A RESOLUTION TO AUTHORIZE A STATE REVOLVING FUND (SRF) LOAN TO THE CONSERVATION FUND (CF) FOR THE BIG RIVER/ SALMON CREEK CONSERVATION FORESTRY ACQUISITION (PROJECT), SRF LOAN NO.: C-06-6090-110

#### WHEREAS:

1. The CF submitted an application for a SRF loan for \$25 million for the project;
2. The Project is consistent with the State Water Resources Control Board's (State Water Board) Antidegradation Policy and will help protect and enhance beneficial uses for waterbodies in the North Coast region;
3. The Project is consistent with the State Water Board's "Plan for California's Nonpoint Source (NPS) Pollution Control Program," and is therefore eligible for SRF funding under Section 319 of the federal Clean Water Act;
4. The Dedicated Source of Repayment for the Project is the revenue derived from the timber harvest consistent with the implementation of the silviculture management measures identified in the NPS Implementation Plan; and
5. It has been determined that the project qualifies for a Class 13 and Class 25 Categorical Exemption from California Environmental Quality Act requirements and will not result in any significant adverse water quality impacts.

#### THEREFORE BE IT RESOLVED THAT:

The State Water Board authorizes a SRF Loan in the amount of \$25,000,000 to the CF for the Big River/Salmon Creek Conservation Forestry Acquisition Project with the condition that the repayment starts one year after the first disbursement.

#### CERTIFICATION

The undersigned, Clerk to the Board, does hereby certify that the foregoing is a full, true, and correct copy of a resolution duly and regularly adopted at a meeting of the State Water Resources Control Board held on July 19, 2006.

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Clerk to the Board